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Capitol Freeze

Fiscal Effects of
Discretionary
Spending Caps



APRIL 2011

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ACKNOWLEDGEMENTS

Ernest V. Tedeschi and Douglas Walton wrote this report. We would like to thank all team members, Laura Fahey, Sarah Holt, Joseph Kennedy, Samantha Lasky, Evan Potler, Carla Uriona and Gaye Williams for providing valuable feedback on the report. Design expertise was provided by Willie/Fetchko Graphic Design. A special acknowledgement to Douglas Hamilton for his guidance and leadership.

The report benefited from the insights and expertise of two external reviewers: Richard P. Emery Jr., former assistant director for budget at the Office of Management and Budget and current consultant for the International Monetary Fund and the World Bank, and Roy T. Meyers, professor of Political Science at UMBC (University of Maryland, Baltimore County). Although they have reviewed the report, neither they nor their organizations necessarily endorse its findings or conclusions.

This report is intended for educational and informational purposes.

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Executive Summary

The United States is on an unsustainable fiscal path. Pew projects that, absent any corrective action, federal debt held by the public will rise to 111 percent of gross domestic product (GDP) in 2025 and reach the unprecedented level of 158 percent of GDP in 2035. Over time, excessive federal debt can raise interest rates, crowd out private capital, stifle productivity and stunt the growth of wages.

The biggest drivers of federal debt growth—by far—are interest payments on the debt and certain “mandatory” programs that Congress need not reauthorize every year, especially Medicare and Medicaid. However, “discretionary” spending—the money that Congress allocates annually to areas such as defense, education and transportation—comprises about 40 percent of the current federal budget. One widely-mentioned option to help rein in deficits and stabilize the debt is a freeze or cap on discretionary spending that still provides policy makers the ability to prioritize spending within broad categories. Individuals and organizations across the political spectrum, including

President Obama and Republicans in Congress, have proposed discretionary spending freezes.

Although the non-partisan Pew Fiscal Analysis Initiative makes no recommendation on a discretionary spending cap, it finds that if policy makers choose to enact such a freeze it could contribute meaningfully to a broader plan for lowering the deficit and debt, but would not solve the problem alone. Pew recognizes, however, that immediate implementation of such a freeze could be a drag on an already fragile economy, and the timing of any fiscal action will be an important consideration. In addition, because a discretionary freeze would result in reduced funding for certain programs which could impact service delivery, policy makers should retain the flexibility to prioritize spending under any freeze.

This report models four freeze options to gauge how much each would save over 10 years. In addition, Pew calculated the 10-year effects of each proposal on the federal deficit and publicly-held debt.

- A five-year freeze of non-security discretionary budget authority at its nominal 2011 level, based on a similar proposal by President Obama in his fiscal year 2012 budget, would save \$377 billion over the next decade, the least amount of the four options.
- An option based on the Republican “Pledge to America” and related legislation would reduce 2011 non-security discretionary budget authority to its inflation-adjusted fiscal year 2008 level and cap growth at the rate of inflation thereafter. It ranks third in overall savings, reducing federal debt by \$400 billion after 10 years.
- The final report of the National Commission on Fiscal Responsibility and Reform proposes a freeze on both security and non-security discretionary budget authority at their nominal fiscal year 2011 levels for one year, with a subsequent rollback to its inflation-adjusted fiscal year 2008 level. This plan would save \$1.5 trillion between 2012 and 2021, more than any other option Pew analyzed.
- Finally, an option included in the report issued by the Bipartisan Policy Center would freeze nominal fiscal year 2011 non-defense discretionary budget authority for four years and defense discretionary budget authority for five years. After that, growth would be limited to increases in the GDP. Forty-eight percent of the savings in this plan would occur by 2016, a higher proportion than in any other option. Overall, it would save \$583 billion over 10 years, the second highest savings of the options Pew analyzed.

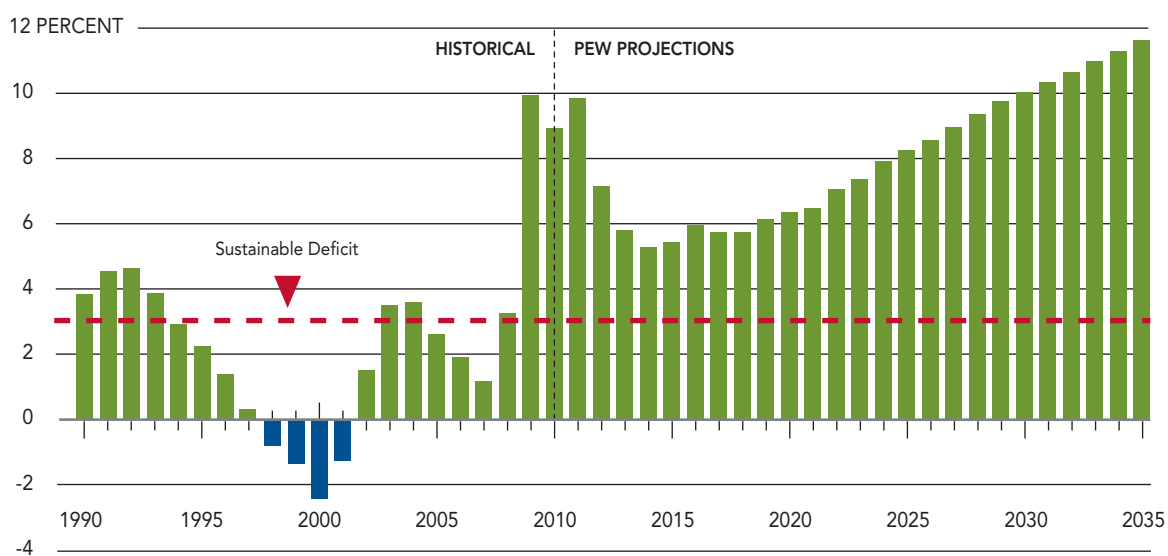
Introduction: Deficits, Debt and the Economy

The recent recession coupled with legislation enacted in the past decade has pushed the federal deficit to historic levels. In fiscal year 2009¹, it reached 9.9 percent of Gross Domestic Product (GDP) (\$1.4 trillion²), the highest relative to the economy since World War II. The deficit declined to 8.9 percent of GDP (\$1.3 trillion) in fiscal year 2010, but

the Congressional Budget Office (CBO) projects that it will rise again to 9.8 percent of GDP (\$1.5 trillion) in fiscal year 2011. Pew projects that the gap between spending and revenues will shrink over the following three years, but will resume growing after fiscal year 2014, reaching 11.6 percent of GDP by 2035 (see Figure 1). These deficit levels are

Figure 1

Unified Federal Budget Deficit as a Percentage of GDP, Fiscal Years 1990 – 2035

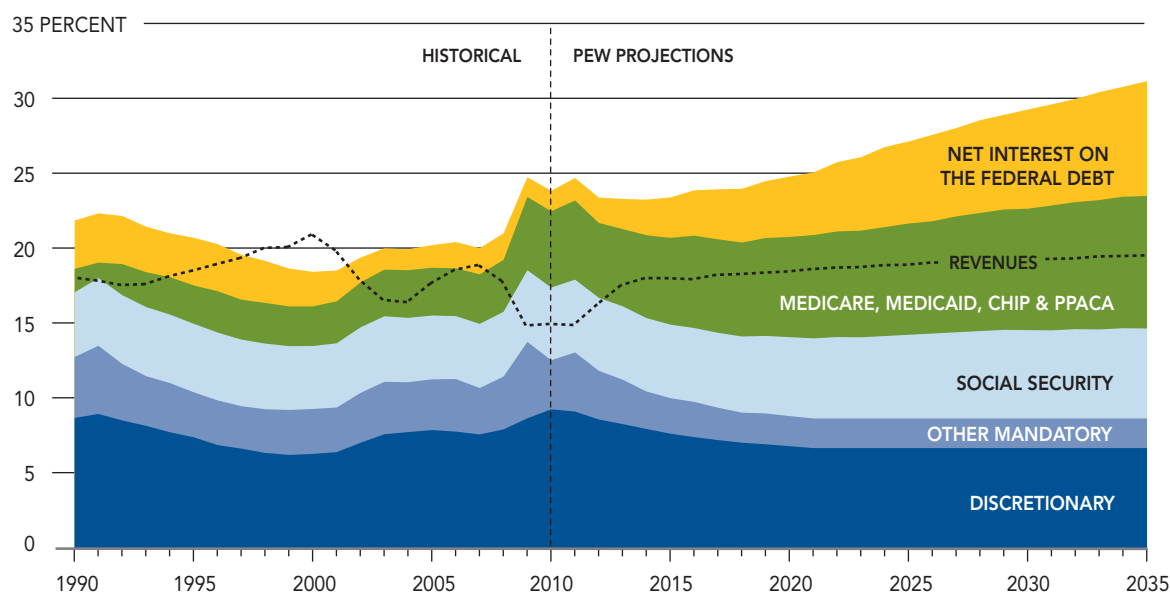


SOURCE: Pew analysis of Congressional Budget Office (2010, 2011) data.

NOTE: "Sustainable Deficit" is the deficit at which publicly-held federal debt is stable as a percent of GDP, equal to roughly 3 percent of GDP.

Figure 2

Federal Revenues and Components of Federal Spending as a Percentage of GDP, Fiscal Years 1990 – 2035



SOURCE: Pew analysis of Congressional Budget Office (2010, 2011) data.

NOTES: "CHIP" refers to spending on the Children's Health Insurance Program. "PPACA" refers to the subsidies and spending on health care exchanges authorized by the Patient Protection and Affordable Care Act of 2010.

significantly higher than the 3-percent-of-GDP-or-less ratio that economists generally recommend for long-term deficits.³ As a result of these deficits, Pew projects that publicly-held federal debt will rise to 111 percent of GDP in 2025 and reach the unprecedented level of 158 percent of GDP by 2035.

The major drivers of spending growth between now and 2035 (other than net interest on federal debt) are Medicare, Medicaid and certain other federal health benefits, as well as to a lesser extent Social Security (see Figure 2). These mandatory

programs made up 42 percent of all federal spending in fiscal year 2010. Pew estimates that their share of spending will rise to 48 percent by 2035. CBO projects that the unavoidable aging of the U.S. population will contribute almost two-thirds of the cost growth in these programs through 2035 (see Figure 3). CBO attributes the remaining one-third to the rapid growth in health care costs. The federal government could choose to cut benefits for future and/or current recipients of Medicare, Medicaid and Social Security. But stabilizing the federal debt at 60 percent of GDP in 2035 by

only cutting mandatory programs would require an immediate and permanent cut of 24 percent in these programs, which would affect current beneficiaries. Furthermore, Congress does not routinely revisit the funding for mandatory programs, and it would be politically difficult for Congress to pass a deficit-reduction plan that relies *exclusively* on cuts in mandatory spending.

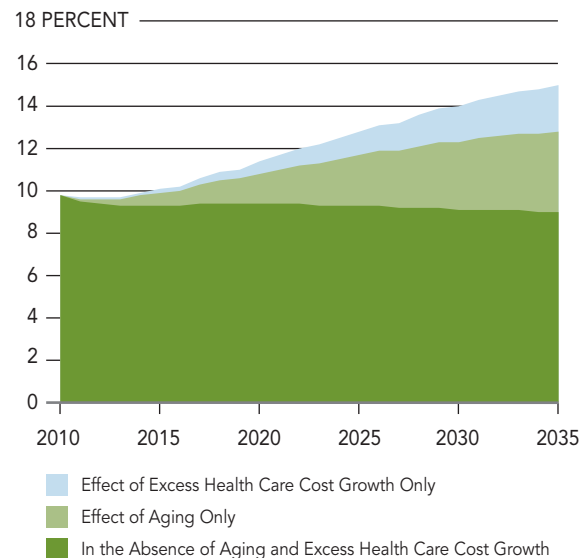
By contrast, federal discretionary spending, which includes most funding for areas such as defense, education, transportation and NASA, is not a long-term deficit driver. CBO projects discretionary spending to shrink as a share of the economy over the next 25 years (see Figure 2). As a share of all federal spending, Pew projects discretionary programs will fall from 39 percent in fiscal year 2010 to 22 percent in fiscal year 2035 as mandatory and interest spending grow. Nevertheless, discretionary spending is still significant—\$1.35 trillion in fiscal year 2010—and because Congress votes on discretionary spending every year, there are more frequent opportunities to make adjustments.

One way Congress could address discretionary spending over the long-term would be to either freeze it in nominal terms (not adjusted for inflation) or cap its annual growth at some benchmark rate. In fact, several policy makers have proposed discretionary freezes. Both

Figure 3

Projected Drivers of Cost Growth in Medicare, Medicaid and Social Security Spending, Fiscal Years 2010 – 2035

Total Medicare, Medicaid and Social Security Spending as a Percentage of GDP



SOURCE: Congressional Budget Office (2009).

NOTE: The interaction effect between excess cost growth and aging has been distributed.

President Obama's fiscal year 2012 budget and the September 2010 Republican Pledge to America propose variations of a discretionary spending freeze.⁴ Recent deficit-reduction plans also include freezes.

However, mechanically applying a discretionary freeze across the board to all categories of spending would deny policy makers the flexibility to shift spending priorities. By contrast, an overall freeze on aggregate discretionary spending accompanied by the flexibility to

make spending adjustments within each category would give policy makers the ability to set funding and policy priorities. Within broad categories of spending, policy makers could adjust funding of individual programs and shift funding between programs, as long as the sum of all spending stayed below the freeze level.

When to cut spending is just as important a consideration as *how* to cut spending. The debate over deficit reduction comes at a time of lingering economic weakness. Even though the recession officially ended in June 2009, according to the National Bureau of Economic Research, unemployment in March 2011 was at 8.8 percent, far from the 5.2 percent CBO considers to be the long-term natural rate of unemployment that occurs during periods of full employment. The Federal Reserve, CBO and the Blue Chip consensus of economic forecasters all project that unemployment will remain at or above 8 percent through 2012.

It is true that high deficits and debt can cause long-term economic damage, but cutting spending too deeply, too soon may derail the recovery. During an economic downturn, there is evidence that temporary deficits that finance tax cuts or spending hikes may help bolster the economy (see Box 1). Similarly,

attacking deficits with tax hikes or spending cuts during a downturn may prolong it by undermining output and employment growth. However, persistent and permanent deficits—and the resulting increase in federal debt—can inflict long-term economic damage by raising interest rates, crowding out private investment, slowing productivity and wage growth and making the U.S. more dependent on foreign lenders. It, therefore, is important for policy makers to guard against both the risks of acting too early to reduce the deficit and debt and the risks of waiting too long.

This report by the Pew Fiscal Analysis Initiative examines the fiscal and economic impacts of a discretionary spending freeze. It models several proposed freeze options to gauge how much each would save over 10 years. In addition, Pew calculated the 10-year effects of each proposal on the federal deficit and publicly-held debt.

Discretionary spending is not a driver of debt growth over the long-term under Pew projections, and no discretionary freeze would be a panacea. Nevertheless, a freeze could be a credible source of deficit reduction if Congress and the president choose to lower the burden borne by benefit cuts and tax hikes.

BOX 1: THE UNCERTAIN MACROECONOMIC EFFECTS OF A DISCRETIONARY SPENDING FREEZE

Pew's analysis of the discretionary spending freezes does not consider how a freeze might effect behavior, productivity or GDP. The decreases in government spending resulting from a discretionary spending freeze likely would have both short-term and long-term macroeconomic effects.

The net marginal effect of government spending on GDP, often called the fiscal multiplier, is a controversial topic in macroeconomics.¹ The conventional economic view is that during a recession when the economy is operating below capacity and the Federal Reserve may be unwilling or unable to counteract an activist fiscal policy, increasing deficit-financed government spending will, on net, bolster real (inflation-adjusted) GDP in the short-term. These positive effects, however, will fade and even turn negative over the long-term as the economy recovers, especially if the federal government does not act to reduce deficits.

There are several empirical studies supporting this view. A 2002 paper by Olivier Blanchard and Roberto Perotti finds that an extra \$1 of government purchases raised real GDP by \$0.50 after one year, a multiplier of 0.5.^{2,3} Alan Auerbach and Yuriy Gorodnichenko find that the multiplier for government spending peaks at 2.5 during a recession and 0.6 during a recovery.⁴ Several macroeconomic models widely used in policy analysis, such as CBO's, also assume positive spending multipliers, implying that spending cuts resulting from a discretionary spending freeze would lower real GDP.⁵

However, Alberto Alesina and Silvia Ardagna⁶ as well as Roberto Perotti⁷ have found that spending cuts enacted during times of fiscal stress (e.g. high deficits) do less harm to the economy and may even cause real GDP to grow. Some studies that find positive multipliers during recessions, such as Auerbach and Gorodnichenko, also find smaller and even negative multipliers during expansions.

Despite uncertainty about the precise effect a discretionary spending freeze would have on employment and output, there is evidence of a risk to the economic growth if government spending were cut too deeply, too soon.

1 For an overview, see Alan Auerbach et al, "Activist Fiscal Policy," *Journal of Economic Perspectives* 24(4), Fall 2010, pp. 141-164.

2 Olivier Blanchard and Roberto Perotti, "An Empirical Characterization of the Dynamic Effects of Changes in Government Spending and Taxes on Output," *Quarterly Journal of Economics* 117(4), Nov 2002, pp. 1329-68.

3 Because government purchases are counted as part of total GDP, a multiplier between 0 and 1 implies that government purchases raise total GDP but partially crowd out private spending.

4 Alan Auerbach and Yuriy Gorodnichenko, "Measuring the Output Responses to Fiscal Policy," NBER Working Paper No. 16311, August 2010.

5 Congressional Budget Office, "Estimated Macroeconomic Impacts of the American Recovery and Reinvestment Act of 2009," March 2009.

6 Alberto Alesina and Silvia Ardagna, "Tales of Fiscal Adjustments," *Economic Policy* 13(27), pp. 487-545.

7 Roberto Perotti, "Fiscal Policy in Good Times and Bad," *Quarterly Journal of Economics* 114(4), November 1999, pp. 1399-1436.

Discretionary Spending and the Federal Budget

When Congress passes a budget, it is actually passing a series of appropriations bills that grant permission to the various parts of the federal government to enter into financial obligations. The amount of obligations into which each agency may enter—basically the amount each agency is allowed to spend—is that agency’s budget authority. What the agency actually spends is an outlay. Although Congress directly controls budget authority, outlays are the appropriate measure of federal spending for the purposes of calculating the effect of a discretionary freeze on the federal deficit and debt. The terms “outlays” and “spending” will be used interchangeably throughout this report (see Box 2 for a glossary of technical terms).

Over the past decade, total federal spending has increased by about 29 percent relative to the economy. In fiscal year 2010, all federal spending totaled about \$3.5 trillion or 23.8 percent of GDP, whereas in fiscal year 2000, federal spending totaled \$1.8 trillion or 18.4 percent of GDP.⁵ Furthermore, over the next 10 years Pew projects that

federal spending will continue its upward trajectory, growing to \$6 trillion, or 25 percent of GDP, by fiscal year 2021.

Federal spending can be divided into three main categories: discretionary, mandatory and interest on the debt.

Congress decides every year how much to spend on discretionary programs through the appropriations process. This includes money to pay for the cabinet departments, such as the Departments of Defense and Transportation, executive branch agencies such as NASA and the ongoing overseas operations in Iraq and Afghanistan. Discretionary spending funds federal programs such as Head Start, Community Development Block Grants, highway construction and new weapons systems. It also covers the day-to-day operating expenses of the federal government, including the salaries of federal workers. Discretionary spending in fiscal year 2010 totaled \$1.35 trillion or about 39 percent of the total federal budget (see Figure 4).⁶ The CBO baseline projects that nominal discretionary spending will grow by an

BOX 2: GLOSSARY OF TERMS

Budget Authority – Amount of financial obligations, designated in annual appropriations laws, that the federal government can enter into that could eventually result in federal outlays.

Outlays – The amount spent (as represented by checks written from the Treasury) by a federal agency to liquidate financial obligations. This report also uses the term “spending” to refer to outlays.

Deficit – The amount by which spending exceeds revenues in a given year.

Publicly-Held Federal Debt – All outstanding U.S. Treasury securities held by nonfederal government entities. The stock of federal debt increases every year by the amount of the deficit plus other means of financing (such as asset sales).

Gross Domestic Product (GDP) – The value of all the goods and services produced within a country’s borders in a given year.

Fiscal Year – The budgeting period of the federal government, which runs from October 1 through September 30.

average annual rate of 1.6 percent between 2010 and 2021 (see Appendix A).

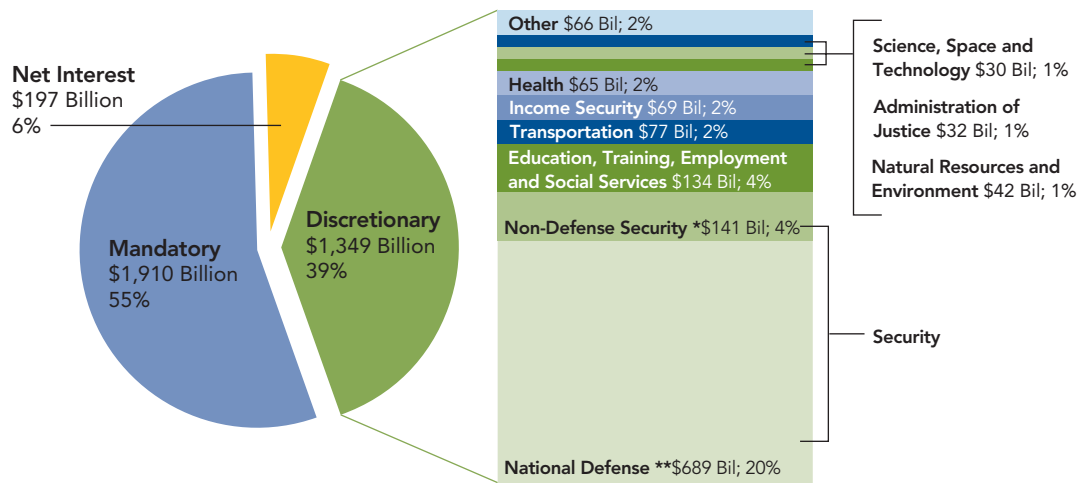
Mandatory spending was \$1.9 trillion, or 55 percent of the federal budget, in fiscal year 2010.⁷ This category of spending includes among other things most federal entitlement programs such as Medicare, Medicaid and Social Security, as well as certain veterans’ benefits, unemployment insurance and the Supplemental Nutrition Assistance Program (SNAP). Unlike discretionary spending, Congress does not need to decide how much to spend on mandatory programs each year; instead, annual spending levels are determined

mostly by eligibility rules, benefit formulas and the participation rate, as well as demographic shifts and changes in the economy. Budget authority for these programs has already been provided under current law and will continue unless and until Congress chooses to change the applicable law. Pew projects average annual growth in nominal mandatory spending to be 5.3 percent over the next 10 years, more than *three times* that of discretionary spending.

The final category, interest on the debt, includes the government’s interest payments on publicly-held federal debt,

Figure 4

Components of Federal Outlays, Fiscal Year 2010



SOURCE: Pew analysis of Congressional Budget Office (2011) data.

*Includes Departments of Homeland Security, State and Veterans Affairs, as well as all remaining components of budget function 150 (international affairs).

**Includes Department of Defense and National Nuclear Security Administration, as well as overseas operations funding.

NOTE: Fiscal year 2010 is the latest fiscal year for which a detailed breakdown of actual outlays is publicly available.

which is all outstanding U.S. Treasury securities held by nonfederal entities, such as banks, sovereign wealth funds and individual investors. The federal government paid \$197 billion in interest on the debt in fiscal year 2010, about 6 percent of the total budget.⁸ Pew projects that rapidly rising debt and higher interest rates over the next decade will cause nominal interest payments to soar, growing at an average annual rate of 15.8 percent over the next 10 years. The federal government can only cut interest payments by reducing federal debt or adjusting monetary policy.

CBO projects that discretionary spending will grow more slowly than interest on the debt or mandatory spending over the next decade. However, a comprehensive plan for stabilizing the debt—including adjustments to discretionary and mandatory spending as well as revenues—will make the necessary remedies easier. Controlling discretionary spending can play a part in a larger plan for reducing deficits and stabilizing the debt and there are several proposals that are being considered by policy makers for addressing growth in this part of the budget.

BOX 3: DISCRETIONARY SPENDING GROWTH

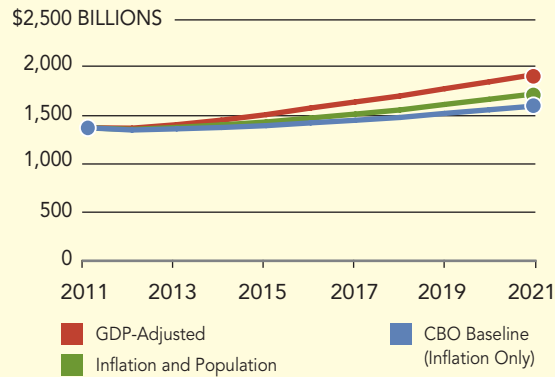
As required by Congress, CBO's January 2011 current law baseline of future discretionary spending assumes that discretionary budget authority grows only at the rate of inflation. CBO makes no judgment in its baseline about the value of different spending, nor does its baseline predict future changes in policy. Some analysts believe that this assumption understates the likely level of future spending growth. Economists Alan Auerbach and William Gale, for example, regularly calculate their own projections of federal spending under the assumption that some discretionary budget authority grows by inflation and population.¹ The Bipartisan Policy Center's Debt Reduction Task Force, headed by Pete Domenici and Alice Rivlin, released a report in November 2010 with a baseline assuming that nominal discretionary budget authority would grow with GDP over the next 10 years.²

Adjusting discretionary budget authority (excluding funding for overseas operations) for inflation and population growth raises cumulative discretionary outlays between 2012 and 2021 by about 4 percent or \$606 billion. Adjusting by GDP growth instead raises cumulative discretionary outlays between 2012 and 2021 by 12 percent or \$1.7 trillion (see figure 5).

Pew's projections of the federal deficit and debt use the CBO current law baseline of discretionary budget authority and outlays, which grows at the rate of

Figure 5

Projections of Nominal Discretionary Outlays Under Three Assumptions, Fiscal Years 2011 – 2021



SOURCE: Pew calculations using Congressional Budget Office (2011) and U.S. Census data.

NOTES: Overseas operations funding is assumed to be the same under all three projections.

"GDP-Adjusted" means that discretionary budget authority grows at the same rate as GDP.

"Inflation & Population Adjusted" means that discretionary budget authority grows at the combined rate of population growth and inflation.

inflation. Using an alternative baseline that assumes discretionary budget authority growing at either inflation and population growth or GDP growth would increase the cost savings of each freeze option analyzed in this report over 10 years relative to the cost savings from applying them to the Pew baseline, but it would not affect the final deficit and debt projections from these options.

1 Alan Auerbach and William Gale, "Tempting Fate: The Federal Budget Outlook," Brookings, 8 February 2011. Note that Auerbach and Gale also significantly adjusted the costs of overseas operations after 2010.

2 Bipartisan Policy Center, "Restoring America's Future," 17 November 2010. Accessed at <http://bit.ly/cIGZtq> on 22 November 2010.

Pew's Methodology for Analyzing Discretionary Freezes

Parameters of Each Freeze Option

Pew modeled the federal fiscal effects of four discretionary spending freeze options, each based on a prominent legislative proposal introduced over the past two years. The options are summarized in Table 1.

Option 1 is based on the freeze proposed in the president's fiscal year 2012 budget. The actual budget proposal is a five-year freeze of fiscal year 2010 nominal non-security discretionary budget authority with growth capped at inflation thereafter.⁹ To make this freeze comparable with others, however, Pew applied it to fiscal year 2011 budget authority rather than fiscal year 2010 as it was originally proposed, and extended the freeze through fiscal year 2016 rather than fiscal year 2015.

Option 2 is based on the freeze described in the 2010 Republican "Pledge to America" and related legislation. Pew applied the freeze to the fiscal year 2012 to 2021 period rather than the 2011 to 2020 period as it was originally proposed

to make it comparable to the other options. Non-security discretionary budget authority for fiscal year 2012 is rolled back to its inflation-adjusted fiscal year 2008 level. Growth thereafter is capped at inflation.¹⁰

Option 3 is the freeze described in the final proposal put forward by the co-chairs of the National Commission on Fiscal Responsibility and Reform, Erskine Bowles and Alan Simpson.¹¹ The co-chairs propose freezing fiscal year 2011 budget authority for both security and non-security discretionary spending for one year, then rolling back fiscal year 2013 discretionary budget authority to its inflation-adjusted fiscal year 2008 levels.¹² Security and non-security budget authority would resume growing again thereafter, with annual growth capped at half of the inflation rate.

Option 4 is taken from a report issued by the Bipartisan Policy Center's Debt Reduction Task Force, chaired by Pete Domenici and Alice Rivlin. The report recommends freezing nominal fiscal year 2011 non-defense discretionary budget authority for four years, and defense discretionary budget authority for five

Table 1

Parameters of the Freeze Options Analyzed by Pew

	What spending is capped or frozen?	What level of budget authority is capped or frozen?	How long does the freeze last?	How is spending capped thereafter?	Pew estimates of total 10-year savings
Option 1 Based on President's FY2012 Budget	Non-security	Nominal FY2011	5 years	Inflation	\$377 billion
Option 2 Based on Republican Pledge to America	Non-security	Real FY2008	N/A	Inflation	\$400 billion
Option 3 National Commission on Fiscal Responsibility and Reform (Bowles-Simpson)	Security and non-security	Nominal FY2011 for first year, then real FY2008	1 year	Half of inflation	\$1,532 billion
Option 4 Bipartisan Policy Center (Domenici-Rivlin)	Defense and non-defense	Nominal FY2011	5 years for defense, 4 years for non-defense	GDP growth	\$583 billion

SOURCE: Pew analysis.

NOTES: All proposals modeled as taking effect beginning in fiscal year 2012.

As written, the president's fiscal year 2012 budget proposes a five-year freeze of nominal fiscal year 2010 non-security budget authority lasting from fiscal years 2011 to 2015. Pew modified this option to freeze fiscal year 2011 non-security budget authority from fiscal years 2012 to 2016 to make it comparable to the other options.

The Pledge to America takes effect in fiscal year 2011 as written. Pew modeled this option as being delayed until fiscal year 2012 to make it comparable to the other options. The Pledge does not include a cost estimate of its proposals.

Defense includes all discretionary spending categorized as budget function 050 (national defense). Non-defense is all discretionary spending not in budget function 050.

Security discretionary spending includes budget functions 050, 150, and the remaining portions of the Departments of Defense, Homeland Security, State and Veterans Affairs. Non-security is all remaining discretionary spending.

years. Growth in budget authority would be capped at GDP growth thereafter.¹³

Each of the four discretionary freeze options is part of a broader package of budgetary recommendations. Except for the policies included in the Pew baseline (see Appendix D), Pew analyzed the freezes in isolation from any other policy

changes to highlight the effects entirely attributable to the freeze. Pew also analyzed each option without making any judgments about the relative effectiveness of different government programs, or to what extent spending cuts and revenue increases should be part of a long-term plan to reduce deficits and the debt.

Modeling Assumptions

The options analyzed in this report are freezes on discretionary budget authority. To estimate the 10-year savings associated with each one, Pew first calculated the direct savings effect relative to the January 2011 CBO current law baseline of discretionary budget authority which Pew did not modify. Pew then applied CBO's 10-year spend-out rate assumptions to convert this budget authority effect into a direct outlay effect.¹⁴ Finally, CBO's 10-year interest rate assumptions were used to calculate the additional savings from reduced interest payments on the debt.

The proposals Pew examines classify discretionary spending in different ways. The proposal from the Bipartisan Policy Commission, for example, uses “defense” and “non-defense” as its spending classifiers. The CBO's January 2011 baseline also distinguishes between defense and non-defense discretionary spending, where defense is defined as all spending within federal budget function 050¹⁵ consisting of the Department of Defense and the Department of Energy's National Nuclear Security Administration. The president's fiscal year 2012 budget, by contrast, distinguishes between “security”

and “non-security” discretionary spending. Security, as defined in the president's budget, is even broader than defense and includes not only the budget function 050, but also the Departments of Homeland Security, State and Veterans Affairs, plus various other international programs (see Figure 4).¹⁶ The other three freeze options analyzed in this report distinguish between security and non-security. In weighing each option, Pew assumed that spending on the operations in Iraq and Afghanistan would not be subject to the freeze.

In determining the effect that the options would have on the deficit and publicly-held debt, Pew used CBO's January 2011 current law baseline for discretionary budget authority and outlays.¹⁷ However, Pew modified the CBO baseline projection for mandatory and net interest spending and revenues to reflect the added costs of permanently adopting certain policies that either have been regularly enacted or are widely expected to be enacted by Congress. Because of the costs associated with these policies, publicly-held federal debt under Pew's baseline is higher over the next 10 years than under CBO's January 2011 baseline. For more information about our methodology, see Appendix D.

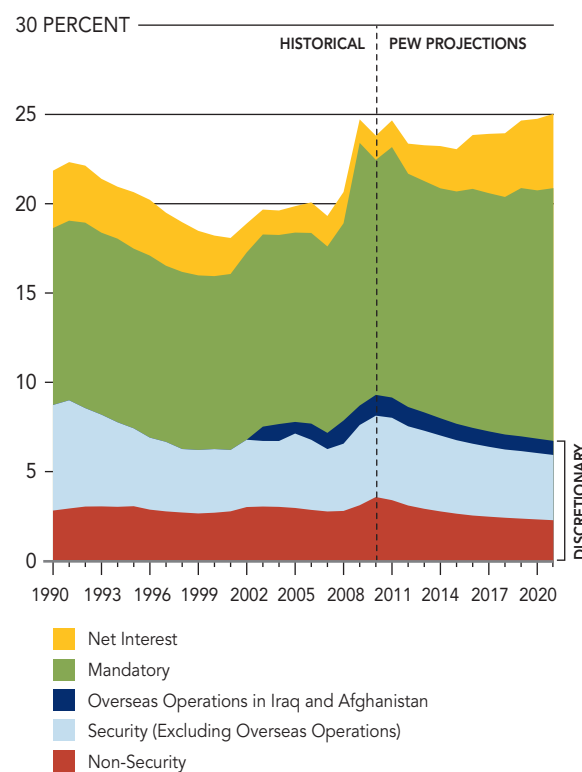
Federal Budgetary Effects of Discretionary Freeze Options Through 2021

As a percent of GDP, total discretionary spending grew by about 47 percent between fiscal year 2000 and 2010, from 6.3 percent to 9.3 percent. The overseas operations in Iraq and Afghanistan represent about 38 percent of this growth, while increases in other security spending comprise 33 percent. Non-security discretionary spending growth is responsible for the remaining 29 percent, almost all of which occurred after 2009. Some of this increase in recent years has been due to recession-related effects and policies, such as falling or stagnant GDP and temporary spending increases. CBO projects that by fiscal year 2021, discretionary spending will fall to 6.7 percent of GDP (see Figure 6 for spending as a percent of GDP). Moreover, as mandatory and interest spending grow, total discretionary spending will become a smaller portion of the federal budget.

Absent any freeze or cap, CBO projects cumulative discretionary spending to total about \$14.5 trillion over the next 10 years. Of this total, \$5.0 trillion will be used for non-security spending, \$7.8 trillion is projected to be spent on security purposes (excluding overseas

Figure 6

Federal Outlays, Fiscal Years 1990 – 2021 (Percent of GDP)



SOURCE: Pew analysis of Congressional Budget Office (2011) and Office of Management and Budget (2011) data.

NOTES: Security discretionary spending includes budget functions 050, 150 and the remaining portions of the Departments of Defense, Homeland Security, State and Veterans Affairs. Non-security is all remaining discretionary spending. Mandatory spending includes Social Security, Medicare, Medicaid, some veterans benefits and any other programs which have permanent budget authority.

operations) and \$1.7 trillion is dedicated to funding for the overseas operations in Iraq and Afghanistan (see Appendix A). For more information on how Pew categorized the CBO baseline by security and non-security spending, see Appendix D.

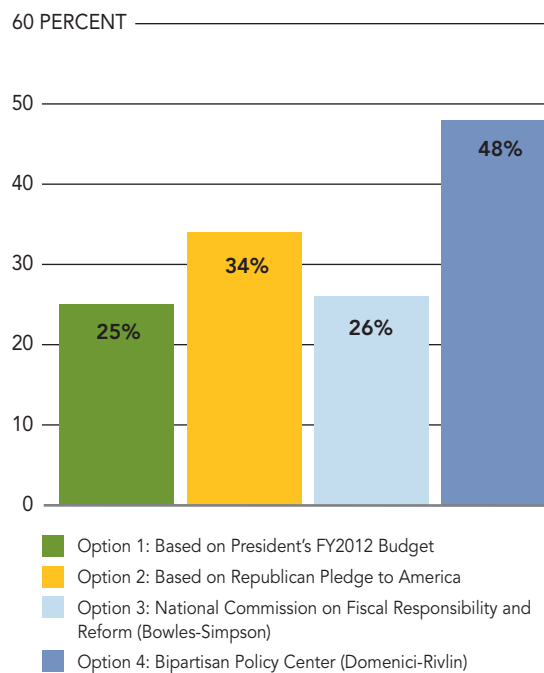
Pew calculated the budgetary savings relative to the CBO current law baseline associated with four discretionary budget authority freeze proposals.

Option 1: Based on President's Fiscal Year 2012 Budget (Freeze 2011 Nominal Non-Security Discretionary Budget Authority Through 2016, Cap Growth at Inflation Thereafter)

Under this option, non-security discretionary budget authority could not exceed its fiscal year 2011 nominal level of \$392 billion between 2012 and 2016. Beginning in 2017, non-security discretionary budget authority would grow annually at the rate of inflation.¹⁸ Over the next 10 years, this option would save a total of \$377 billion in direct and interest spending (see Appendix B), 25 percent of which would be realized by 2016 (see Figure 7). This would be the equivalent of cutting non-security discretionary spending permanently and immediately by 5.5 percent beginning in fiscal year 2011.¹⁹ This proposal saves the least through fiscal year 2021 of the four options Pew analyzed.

Figure 7

Proportion of 10-Year Savings from Different Freeze Options Accruing from 2012 – 2016



SOURCE: Pew analysis of Congressional Budget Office (2011) data.

Option 2: Based on Republican Pledge to America (Roll Back and Cap Non-Security Discretionary Budget Authority)

This option would cut fiscal year 2012 non-security discretionary budget authority to its inflation-adjusted fiscal year 2008 level of \$372 billion, reducing discretionary budget authority by \$26 billion that year alone. Growth in budget authority thereafter would be capped at inflation. Between fiscal years 2012 and 2021, this approach ranks

third in savings among the four options Pew analyzed, saving about \$400 billion in direct spending and interest outlays. Thirty-four percent of this (\$135 billion) would occur by 2016, the highest proportion of the four. This option's 10-year savings would be the equivalent of immediately and permanently cutting non-security discretionary spending by 5.8 percent beginning in fiscal year 2011.

Option 3: National Commission on Fiscal Responsibility and Reform Final Proposal (Roll Back, Reduce and Cap All Discretionary Budget Authority Except Overseas Operations)

The final proposal put forward by the co-chairs of the National Commission on Fiscal Responsibility and Reform contained a discretionary freeze that included the following: a) keeping fiscal year 2012 discretionary budget authority (excluding overseas operations) at nominal 2011 levels; b) cutting fiscal year 2013 discretionary budget authority to inflation-adjusted 2008 levels; and c) capping growth thereafter at half the rate of inflation. This approach would save \$1.5 trillion in direct and interest outlays between 2012 and 2021, by far the most of the four options. Interestingly, 26 percent of savings accrue by 2016, only 1 percentage point higher than the president's plan. The commission's freeze proposal would be the equivalent of immediately and permanently cutting all

discretionary spending, excluding overseas operations costs, by 8.8 percent beginning in fiscal year 2011.

Option 4: Bipartisan Policy Center (Freeze Nominal Budget Authority for Four or Five Years, Cap Growth Thereafter at GDP)

The Bipartisan Policy Center's (BPC) Debt Reduction Task Force proposed a four-year nominal freeze on non-defense discretionary budget authority and a five-year freeze on defense discretionary budget authority. Growth in budget authority would be capped at GDP growth afterwards. It is important to note that BPC used a baseline whereby discretionary budget authority increased by GDP rather than inflation over the next 10 years, so BPC's proposal yields greater savings under their assumptions than under CBO's baseline.

Nevertheless, Pew calculated that this option would save \$583 billion in direct and interest outlays through 2021, the second highest 10-year savings of the four options. About \$280 billion (48 percent) of these savings would be accrued by 2016. The BPC approach would be the equivalent of immediately and permanently cutting all discretionary spending, excluding overseas operations costs, by 3.3 percent beginning in fiscal year 2011.

Effects of the Freeze Options on the Deficit and the Debt

Without a freeze on discretionary spending, Pew's baseline assumes deficits in excess of 5 percent of GDP for the next 10 years (see Figure 8). Five of the next 10 years have projected deficits above 6 percent of GDP under Pew's baseline. Each of the four discretionary freeze options would reduce the deficit, but none of the options alone would be sufficient to meet the National Commission on Fiscal Responsibility and Reform's goal of lowering the deficit to 3 percent of GDP by fiscal year 2015. Option 3, the freeze in the final proposal from the National Commission's co-chairs, would have the greatest effect on the long-term deficit, lowering the deficit in 2021 from 6.5 percent of GDP under the Pew baseline to 5.2 percent of GDP. However, if policy makers choose, any one of these proposals could be part of a larger package of remedies to cut the deficit and lower the debt.

Without a freeze, the federal debt would grow to 97 percent of GDP in 2021 under Pew's baseline (see Figure 9). The different options would have varying effects on the debt. Both Option 1 (the president's proposed spending freeze) and Option 2

(the Pledge to America's rollback and freeze) would have similar effects, lowering federal debt in 2021 to about 95 percent of GDP. By contrast, Option 3 (the National Commission's proposal) would lower debt in 2021 to 91 percent of GDP. The options that would freeze both defense and non-defense discretionary budget authority (or security and non-security) would have larger effects than those that only froze non-defense or non-security budget authority.

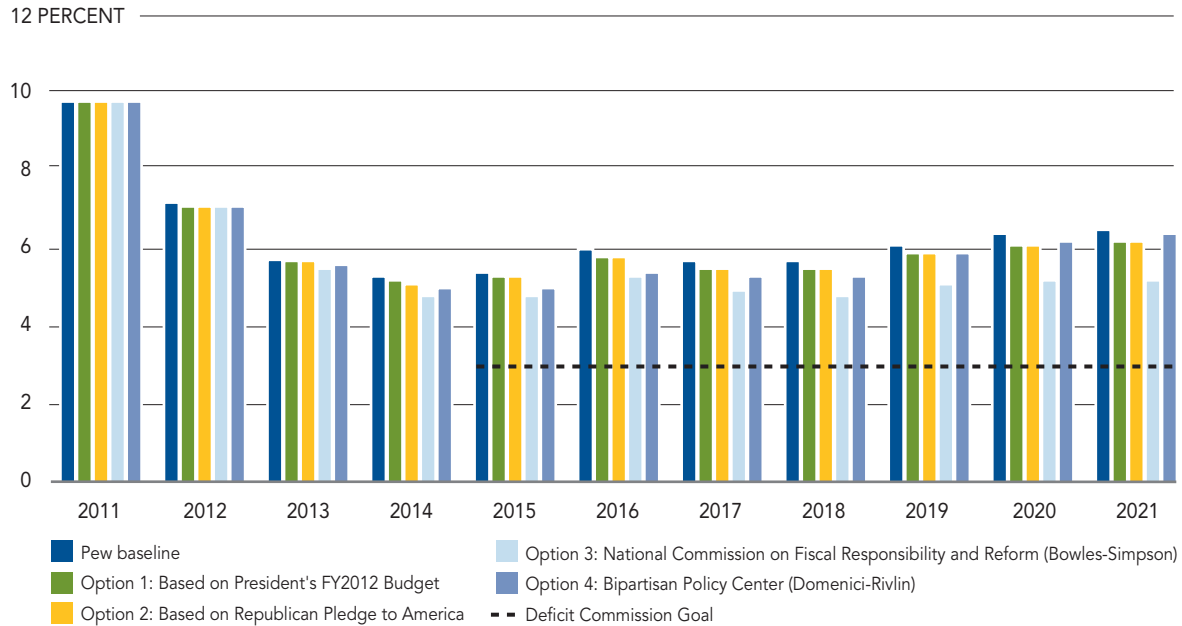
Under any of the four options, however, federal debt still would be on an upward trajectory, and none of the individual options alone would achieve a debt-to-GDP ratio of 60 percent as recommended by the European Union, the International Monetary Fund, the Peterson-Pew Commission on Budget Reform and the National Academy of Public Administration.

What Budget Areas Would Be Affected the Most by a Freeze?

Different programs and policy areas have grown at different rates in recent history,

Figure 8

Federal Deficits Under the Freeze Options, Fiscal Years 2011 – 2021, Percent of GDP



SOURCE: Pew analysis of Congressional Budget Office (2011) data.

NOTES: Pew baseline is based on the January 2011 CBO baseline modified to reflect the additional costs of four policies: (1) permanent extension of the 2001/2003 tax cuts for all individuals; (2) indexing the 2009 parameters of the Alternative Minimum Tax to inflation; (3) permanent extension of the parameters of the estate and gift taxes enacted as part of the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010; and (4) permanently overriding cuts to Medicare physician reimbursements scheduled under the Sustainable Growth Rate.

"Option 1" is a freeze of nominal 2011 non-security discretionary budget authority through 2016, with growth capped at inflation thereafter.

"Option 2" is a rollback of 2012 non-security discretionary budget authority to real 2008 levels, with growth capped at inflation thereafter.

"Option 3" is a nominal freeze of all non-war 2011 discretionary budget authority through 2012, with a rollback to inflation-adjusted 2008 budget authority in 2013 and growth capped at half of inflation thereafter.

"Option 4" is a nominal freeze of non-defense discretionary budget authority for four years and defense discretionary budget authority for five years, with growth capped at GDP thereafter.

"Deficit Commission Goal" refers to the mission of the National Commission on Fiscal Responsibility and Reform as laid out in Executive Order 13531 of February 18, 2010. The commission's goal was to propose recommendations bringing the federal deficit to primary balance—about 3 percent of GDP—by 2015.

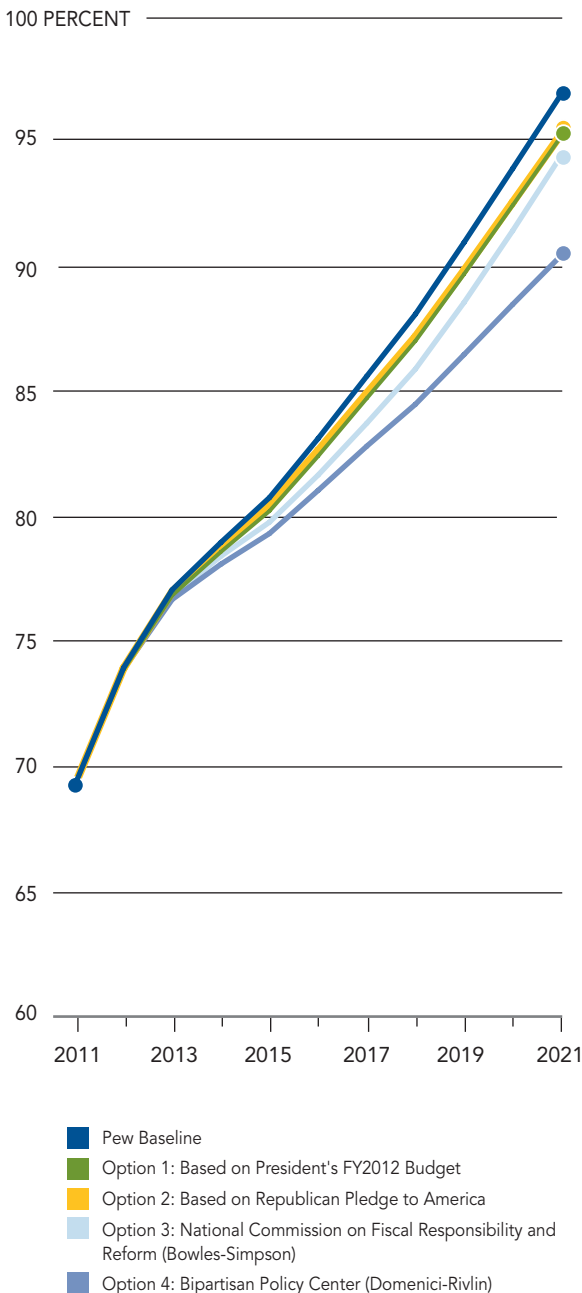
and the same will hold true over the next 10 years. By extension, a spending freeze would also have different fiscal impacts depending on the areas being targeted. Pew used CBO January 2011 baseline projections to apply a function-by-function nominal freeze from fiscal

years 2012 to 2021 (see Appendix C). Pew assumed that Congress does not shift funding between budget functions.

The budget area that would see the greatest cumulative cut in nominal terms over 10 years would be National Defense

Figure 9

U.S. Publicly-Held Debt as a Percent of GDP Under the Freeze Options, Fiscal Years 2011 – 2021



SOURCE: Pew analysis of Congressional Budget Office (2011) data.

NOTE: Only includes the effects of the discretionary spending freezes in each proposal.

(budget function 050), whose outlays would fall \$773 billion through 2021. In relative terms, this is about 10 percent of CBO's projected cumulative outlays for National Defense between fiscal years 2012 and 2021. By comparison, Commerce (budget function 370) would see only a \$22 billion cumulative nominal cut through 2021; however, this represents more than half of its projected outlays during this period. The effects of a nominal freeze vary by function due to 1) different CBO assumptions of the 10-year growth in each agency's budget authority, and 2) accounting variations specific to each budget area (for example, negative budget authority resulting from federal guarantees of mortgage-backed securities).

The results also illustrate that the broader the freeze, the larger the long-run savings. A 10-year nominal freeze that only applied to non-defense spending, for example, would save about \$573 billion by 2021, not counting interest savings. By expanding the freeze to include defense spending in this instance, the 10-year savings would more than double.

BOX 4: FISCAL EFFECTS OF REDUCING OR ELIMINATING SPENDING ON OVERSEAS OPERATIONS

CBO's current law baseline assumes that future annual appropriations for the overseas operations in Iraq and Afghanistan will grow with inflation. Thus, the \$159 billion in fiscal year 2011 budget authority for overseas operations stays constant in real terms through 2021 under CBO assumptions. This means that the CBO baseline assumes there will be no combat troop reductions in Iraq and Afghanistan between 2011 and 2021.

What if, however, overseas operations were cut or eliminated? In CBO's January 2011 Budget and Economic Outlook, there is a cost estimate of an alternative option to reduce the number of troops in Iraq and Afghanistan from their current level of 220,000 to 45,000 by 2015.¹

As with discretionary spending freezes, cutting funding for overseas operations would not stabilize the debt by itself, but it would have a meaningful effect on future deficits. CBO estimates that reducing overseas personnel to 45,000 by 2015 would cut direct and interest outlays by about \$1.3 trillion dollars over 10 years relative to the Pew baseline and reduce federal debt in 2021 from 97 percent of GDP to 91 percent. Pew found that this option lowered federal debt by almost as much as eliminating all war funding by 2015.

¹ Congressional Budget Office, *The Budget and Economic Outlook*, January 2011, p. 23.

Conclusion

America's fiscal trajectory is unsustainable, and federal policy makers likely will consider a broad range of options to reduce deficits and stabilize the debt. These include revenue increases and cuts in long-term debt drivers such as Medicare and Social Security. They also might include cuts or freezes on discretionary spending, which is not a long-term debt driver but could contribute to a larger plan. Policy makers should consider that even though the economy has been out of recession since June 2009, a premature cut in federal spending might have a negative impact on the nascent economic recovery. The risk of slower economic growth from spending cuts is higher in the short-term but fades over the long-term, especially after the economy returns to full

employment; by contrast, the economic risks from growing deficits and debt are smaller in the short-term but grow over the long-term.

Although Pew makes no recommendations, the analysis of the four proposed freeze options demonstrates that limits on discretionary spending could yield meaningful budget savings. The results also suggest that the broader the freeze, the greater the impact. Although even the broadest freeze Pew analyzed was not sufficient by itself to stabilize long-term federal debt, controlling discretionary spending growth could play a role in a broad solution to the federal government's fiscal problems.

Appendix A

Components of Federal Outlays, Fiscal Year 2010

	Category	Description	FY2010 Outlays	Percent of FY2010 Outlays	Average Annual Nominal Growth Pew Projections, 2011 – 2021
DISCRETIONARY	Overseas Operations	Operations in Iraq and Afghanistan	\$169 billion	4.9%	1.0%
	Security (Excluding Overseas Operations)	Security-related discretionary spending	\$661 billion	19.1%	2.1%
	Non-Security	All other discretionary spending	\$519 billion	15.0%	0.9%
	MANDATORY	Includes federal entitlement programs	\$1,910 billion	55.3%	5.3%
	INTEREST ON THE DEBT	Interest payments on outstanding publicly-held Treasury securities	\$197 billion	5.7%	15.8%

SOURCE: Pew analysis of Congressional Budget Office (2011) data.

CBO Baseline of Discretionary Budget Authority and Outlays, Fiscal Years 2011 – 2021 (in billions of dollars)

Budget Authority Baseline	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2012-21
Overseas Operations	159	161	163	166	169	172	175	179	182	186	189	1,741
Security (Excluding Overseas Operations)	704	714	728	744	761	779	801	823	845	868	890	7,954
<i>Defense (050) Excluding War</i>	551	560	571	584	597	611	628	645	663	680	698	6,237
<i>Non-Defense Security</i>	154	154	157	161	164	168	173	178	183	188	192	1,717
Non-Security	392	398	405	414	423	432	443	455	466	478	490	4,404
TOTAL	1,255	1,272	1,297	1,324	1,352	1,383	1,419	1,456	1,494	1,532	1,570	14,099

Outlays Baseline	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2012-21
Overseas Operations	170	170	168	167	167	170	173	176	180	184	188	1,743
Security (Excluding Overseas Operations)	693	696	717	734	749	770	784	800	826	848	870	7,793
<i>Defense (050) Excluding War</i>	541	540	557	571	585	603	614	625	647	664	681	6,088
<i>Non-Defense Security</i>	152	156	160	162	164	167	170	175	179	184	189	1,706
Non-Security	511	487	478	478	481	486	496	506	518	530	542	5,001
TOTAL	1,375	1,352	1,364	1,378	1,397	1,426	1,453	1,482	1,524	1,562	1,600	14,538

SOURCE: Pew calculations using Congressional Budget Office (2011) data.

NOTES: "Overseas Operations" includes the costs of the operations in Iraq and Afghanistan. "Security" spending includes all non-war spending in 1) budget function 050 (National Defense); 2) budget function 150 (International Affairs); and 3) all spending in the Departments of Homeland Security, State and Veterans Affairs not classified under budget functions 050 or 150.

Appendix B

Budget Authority and Outlay Savings from Four Discretionary Freeze Proposals, Fiscal Years 2011 – 2021 (in billions of dollars)

The table below shows the savings in budget authority and outlays from each of the four proposals Pew analyzed, as well as total five-year and 10-year savings.

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2012-2016	2012-2021
Option 1: Based on President's FY2012 Budget													
Change in Non-Security BA	0	6	14	22	31	41	44	47	51	54	58	114	367
Change in Outlays	0	3	9	17	26	36	44	51	57	63	70	93	377
Change in Direct Costs	0	3	9	17	25	34	40	44	48	51	55	87	324
Change in Interest	0	0	0	1	1	3	5	7	9	12	15	5	53
Option 2: Based on Republican Pledge to America													
Change in Non-Security BA	0	26	28	30	33	35	38	41	45	48	51	151	374
Change in Outlays	0	14	23	28	33	37	42	47	53	59	65	135	400
Change in Direct Costs	0	14	22	26	30	33	36	39	42	45	48	125	335
Change in Interest	0	0	1	2	3	4	6	8	11	14	16	10	65
Option 3: National Commission on Fiscal Responsibility and Reform (Bowles-Simpson)													
Change in Non-Security BA	0	6	28	33	39	45	52	59	67	75	83	151	487
Change in Security BA	0	10	59	69	80	93	107	123	138	153	169	312	1,002
Change in Outlays	0	9	55	86	111	136	163	193	225	259	295	397	1,532
Change in Direct Costs	0	9	54	83	104	123	144	165	188	210	233	373	1,314
Change in Interest	0	0	1	3	7	12	19	28	37	49	62	24	219

* Continued on next page

Appendix B – continued

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2012-2016	2012-2121
Option 4: Bipartisan Policy Center (Domenici-Rivlin)													
Change in Non-Security BA	0	7	17	29	42	27	16	5	-6	-18	-31	122	88
Change in Security BA	0	11	25	40	56	73	60	48	35	20	5	205	373
Change in Outlays	0	10	30	55	84	101	96	83	65	43	17	280	583
Change in Direct Costs	0	10	29	53	79	93	83	65	43	19	-8	263	466
Change in Interest	0	0	1	2	5	9	13	18	21	24	26	16	118

SOURCE: Pew analysis of Congressional Budget Office (2011) data.

NOTES: "Option 1" is a five-year freeze of nominal fiscal year 2011 non-security discretionary budget authority beginning in fiscal year 2012, with growth capped at inflation thereafter.

"Option 2" is a rollback of fiscal year 2012 non-security discretionary budget authority to inflation-adjusted fiscal year 2008 level, with growth capped at inflation thereafter.

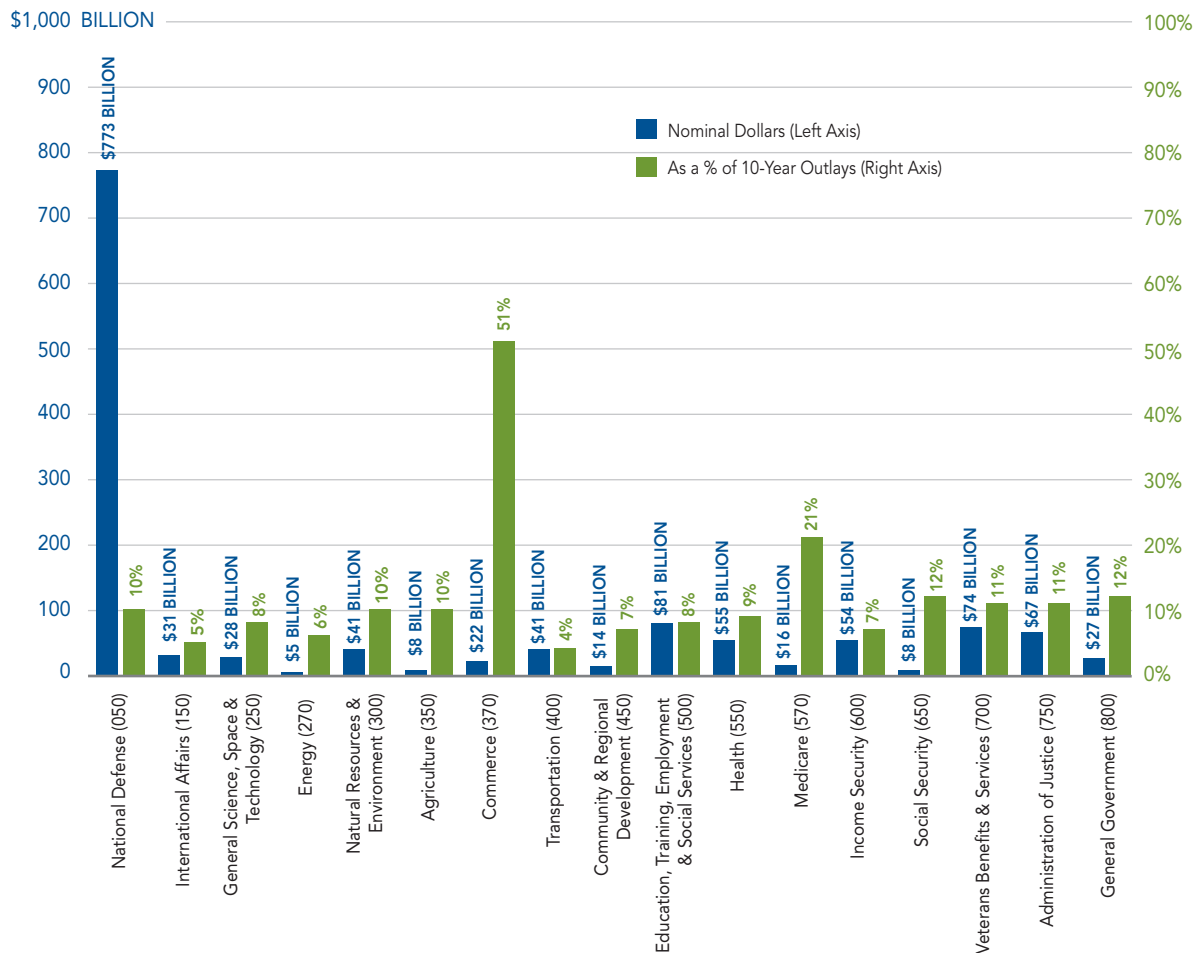
"Option 3" is a) a one-year freeze of nominal fiscal year 2011 non-security discretionary budget authority; b) a cut of fiscal year 2013 non-security discretionary budget authority to inflation-adjusted 2008 levels; and c) growth in fiscal year 2014 and beyond capped at half of inflation.

"Option 4" is a five-year freeze of nominal defense discretionary budget authority beginning in fiscal year 2012 and a four-year freeze of nominal non-defense discretionary budget authority beginning in fiscal year 2012, with growth capped at GDP growth thereafter.

Appendix C

Cumulative Cut Resulting from a 10-Year Nominal Freeze of Budget Authority, in Billions of Dollars and as a Percent of Cumulative 2012 – 2021 Projected Outlays Under the CBO January 2011 Baseline

The chart below shows how spending in each budget function would fare if nominal fiscal year 2011 budget authority were frozen for 10 years and if policy makers were not allowed to transfer funding between budget functions.



SOURCE: Pew analysis of Congressional Budget Office (2011) data.

NOTE: The discretionary portions of Medicare (budget function 570) and Social Security (budget function 650) are primarily administrative costs. A discretionary spending freeze would not directly affect benefit payments authorized for mandatory programs.

Technical Appendix

For projecting federal debt and deficit levels over the next 10 years, Pew's analysis uses a budget model based on data from the Congressional Budget Office (CBO). The model projects budget authority, outlays, deficit and debt at the end of each federal fiscal year.

Model Framework

Components of Pew's budget model are described in the sections below.

Non-Interest Outlays, Budget Authority and Revenue

Non-interest spending categories used in this model include Social Security, Medicare net of offsetting premiums, other federal medical outlays (which include Medicaid, the Children's Health Insurance Program and health exchange subsidies), other mandatory outlays and total discretionary budget authority and outlays. The revenue categories include personal income tax, corporate income tax, social insurance taxes on wages and other revenue. Data for primary spending and revenue are drawn from the January 2011 *Budget and Economic Outlook* from the CBO.

For projections through 2021, Pew creates a baseline that reflects the CBO current-law baseline, with four permanent policy adjustments that have been historically extended by Congress:

- Index the Alternative Minimum Tax (AMT) to inflation;
- Provide annual patches to prevent scheduled cuts in Medicare physician payment rates under the Sustainable Growth calculation;
- Extend the 2001 and 2003 tax cuts for all individuals; and
- Extend the estate and gift taxes under the parameters included in the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (Public Law 111-312).

Pew's baseline projection assumes that these four policies are enacted without offset for the entire fiscal year 2012 to 2021 period. Pew estimates that these policies would increase federal debt by more than \$4.8 trillion over the next 10 years if they are not offset by other spending cuts or tax increases.

Interest

This model uses the interest rates implied by the CBO baseline, which is found by dividing net interest by the average of debt held by the public at the beginning of the year and at the end of the year. Net interest is calculated under different policy scenarios by multiplying the interest rates described above by the average level of debt held by the public each year.

Other Means of Financing (OMF)

OMF includes various factors that reduce or increase the government's need to borrow. A sale of assets, for example, provides the government with additional funds and reduces its need to borrow to finance its deficit; this is recorded as a negative OMF value. Certain credit financing, however, increases the government's need to borrow, and is recorded as a positive OMF value. In Pew's baseline, OMF is equal to the level specified in the CBO January 2011 baseline.

Debt and Deficit

Future levels of deficit and debt are derived from the component pieces of the model. The deficit is equal to total outlays less total revenues. Debt held by the public is equal to debt at the beginning of the year, plus the deficit and OMF. This framework enables the model to calculate debt and deficit at the end of each fiscal year.

Policy Simulations

This report examines how various discretionary freeze options would affect the federal debt and deficit. The CBO baseline categorizes discretionary budget authority and outlays by defense and non-defense. For the freeze options involving security and non-security spending freezes, Pew recategorized the discretionary budget authority and outlay totals in the CBO's January 2011 baseline between these various spending categories. Pew used a detailed version of CBO's January 2011 baseline to reallocate spending, then used the Public Budget Database of outlays and budget authority from the Office of Management and Budget (OMB) to check for consistency.

For simulations involving changes in budget authority, Pew used the CBO's August 2010 spend-out rate assumptions for defense and non-defense discretionary budget authority to derive the outlay effects. Pew reweighted these spend-out rates for use with security and non-security discretionary budget authority.

The model adjusts future discretionary budget authority or outlays based on the specifications of each freeze. All other non-interest spending and revenue remain the same as the Pew baseline while interest is endogenously determined using the implied interest rate. The model then calculates future debt and deficit levels based on these adjusted levels of outlays. As in all the simulations, the interest rate and GDP are the same as in the Pew baseline.

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Office of Management and Budget, Public Budget Database of Outlays: Fiscal Year 2012. OMB, January 2011.
Obtained at <http://www.whitehouse.gov/omb/budget/Supplemental> on 14 February 2011.

Endnotes

1 Federal fiscal years begin on October 1 and end on September 30.

2 All dollar figures presented in this report are nominal, i.e. not adjusted for inflation.

3 See for example Mike Dorning, “Orszag Seeks Budget Deficit of 3 Percent of GDP in Six Years,” *Bloomberg*, 17 November 2009. Obtained at <http://bloom.bg/hqxdta> on 24 January 2011.

4 “A Pledge to America: The Republican Agenda.” Access at <http://pledge.gop.gov/> on 20 October 2010.

5 Office of Management and Budget (2011).

6 Ibid.

7 Ibid.

8 Ibid.

9 The source for the parameters of Option 1 was Office of Management and Budget, *Budget of the United States Government – Fiscal Year 2012*, February 2011. The Office of Management and Budget’s own estimate of the direct and interest savings from the president’s proposed freeze as written in the fiscal year 2012 budget is \$406 billion over 10 years.

10 See Note 4. Pew also consulted S. 3779, introduced on 14 September 2010, for its analysis of Option 2.

11 National Commission on Fiscal Responsibility and Reform, *The Moment of Truth*, December 2010. Obtained at <http://goo.gl/K8F2m> on 24 February 2011.

12 The co-chairs propose categorizing discretionary budget authority either by security/non-security or defense/non-defense. Pew chose to model its freeze as one on security and non-security budget authority.

13 Bipartisan Policy Center Debt Reduction Task Force, *Restoring America’s Future*, 17 November 2010. Obtained at <http://bit.ly/cIGZtq> on 24 November 2010.

14 Pew used the CBO’s August 2010 10-year spend-out rate assumptions for defense and non-defense discretionary budget authority. Pew reweighted these spend-out rates to use for security and non-security discretionary budget authority.

15 Budget functions are accounting categories of federal spending with similar uses. For example, budget function 050 covers national defense spending, and includes the Department of Defense as well as some spending outside the Department of Defense, such as the Department of Energy’s National Nuclear Security Administration.

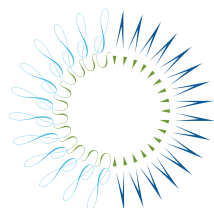
16 See Office of Management and Budget, *Budget of the United States Government – Fiscal Year 2012*, February 2011, Table S-11. Security discretionary spending includes the discretionary components of the Departments of Defense, Homeland Security and Veterans Affairs, the National Nuclear Security Administration, and budget function 150, which includes the Department of State and other international programs. In the past, the federal government has categorized the components of discretionary spending differently. For example,

the 1990 Budget Enforcement Act (BEA) defined three categories of discretionary spending: defense, international affairs and domestic. See Title XIII of the Omnibus Budget Reconciliation Act of 1990 (Public Law 101-508). The 1997 amendments to the BEA reduced the number of categories to two: defense and non-defense, where defense included only the Department of Defense and the National Nuclear Security Administration. See Title X of the Balanced Budget Act of 1997 (Public Law 105-33). The savings from freezing or capping a category of discretionary spending varies depending on how broadly or narrowly that category is defined. In general, the narrower the target of a freeze, the smaller the long-term budget savings.

17 Congressional Budget Office (2011), p. 21.

18 Pew used the CBO's January 2011 forecast of the GDP price index as its measure of inflation for each option.

19 "Equivalent cuts" for each option show the percentage permanent cut to that option's spending base in 2011 sufficient to bring the debt-to-GDP ratio to the same level in 2021 as the option itself. Pew assumes that spending grows at its baseline rate (inflation) after the cuts in 2011.



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